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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1996

NEW VALLEY CORPORATION,

Petitioner,

—v.—

NEW VALLEY CORPORATION SENIOR EXECUTIVE BENEFIT PLAN PARTICIPANTS, AND WALTER E. GIRARDIN, ALEXANDER J. CHISHOLM, S.E. SMISZKO, JOHN A. HUNT, ARTHUR GARMAN, GERALD P. KENT, DELMAR HARMON, ROBERT R. GARBARINI, WALTER L. ELKINS, PHILIP SCHNEIDER, J. WILLIAM HARRINGTON, JOHN A. HOLLANSWORTH, BERNARD WEITZER, JOHN W.R. POPE, JR., ROBERT M. FLANAGAN, DOUGLAS D. LLOYD, H.E. SALTER/BARBARA ORR SALTER, RICHARD L. CALLAGHAN, AND RUSSELL W. MCFALL,

Respondents.

ON PETITION FOR WRIT OF CERTIORARI TO
THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

REPLY BRIEF

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Respondents.

REPLY BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

Respondents do not dispute that the Court of Appeals for the Third Circuit has enabled top hat plan participants to proceed to trial on claims for retirement benefits that would be dismissed as a matter of law if brought by ordinary welfare plan participants. Respondents instead contend that, in light of the exemption of top hat plans from various statutory requirements applicable to other employee benefit plans, this Court need not be concerned with the methodology used to reach this absurd result. Notwithstanding the statutory exemptions, however, the Third Circuit ultimately construed the Senior Executive Benefit Plan ("SEBP") and Girardin Plan (collectively, the "Plans") based on the same federal common law principles that have been endorsed

by some courts, and rejected by others, in construing employee benefit plans generally. Insofar as it used these principles to enhance the rights of top hat plan participants notwithstanding the contrary intent of the legislature, the decision underscores the need for resolving the conflict among the circuits over the appropriate use and application of ERISA federal common law.

Respondents' alternative contention, that there are no conflicts among the circuits regarding the construction of reservation-of-rights clauses or the use of ERISA federal common law principles, is baseless. Although Respondents quibble over precisely what method of construction was employed in certain of the cases cited, and whether the methodology used in particular cases was determined by the unique facts and circumstances presented, there can be no disputing that several different rules of construction are presently being employed by the courts. This effectively undermines the congressional goal of uniformity in the construction of employee benefit plans, which this Court could restore by granting a writ of certiorari.

I.

NOTWITHSTANDING THE UNIQUE FEATURES OF TOP HAT PLANS, THE DECISION BELOW IS PREMISED ON THE LOWER COURT'S ENDORSEMENT OF FEDERAL COMMON LAW PRINCIPLES

In their Brief in Opposition ("Opp."), Respondents contend that the Third Circuit's decision derives from the unique status of top hat plans and, therefore, that the authorities cited by New Valley to establish a split among the circuits on the use of common law principles of plan construction are irrelevant. (*See* Opp. at 2-5) A close reading of the decision reveals, however, that, notwithstanding the inapplicability of certain statutory provisions to top hat plans, the Third Circuit applied principles of federal common law used to construe employee benefit plans generally. This case provides a perfect opportunity to resolve the question as to whether these principles, or other rules of

construction, should uniformly govern the construction of employee benefit plans.

The Third Circuit's observation that top hat plans are not governed by ERISA's writing requirement, and thus that the terms of such plans may be established orally, ultimately does not control the court's methodology for construing the Plans.[1] The court did not rule, for example, that extrinsic evidence should be considered for purposes of determining whether the Plans were orally modified. Rather, the court directed that extrinsic evidence be considered strictly for purposes of construing the *written* terms of the Plans. In fact, notwithstanding the court's initial observations regarding the inapplicability of the writing requirement, the entire opinion is devoted to an analysis of whether the written terms of the Plans are unambiguous, and whether extrinsic evidence should assist in making that determination. In performing that analysis, the court applied the same principles of contract construction used elsewhere by some courts, and rejected by other courts, in construing other types of employee benefit plans. (*See* A-11)

The Third Circuit's reference to *Carr v. First Nationwide Life Ins. Co.*, 921 F. Supp. 1476 (N.D. Cal. 1993), does not, as

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[1] The notion that the inapplicability of ERISA's writing requirement should have a bearing on the methodology used to construe top hat plans is belied by the fact that, even before ERISA's enactment, courts routinely applied a "plain meaning" rule of construction, and found reservation-of-rights clauses to be unambiguous as a matter of law, notwithstanding the absence of any statutory provision operating as an integration clause. *See, e.g., Kolentus v. AVCO Corp.*, 789 F.2d 949 (7th Cir. 1986) (reservation-of-rights clause precluded finding of intent to vest); *Boase v. Lee Rubber & Tire Corp.*, 437 F.2d 527 (3d Cir. 1970) (ruling that, under New York common law of contract, reservation-of-rights clause in pension plan renders promise of lifetime benefits conditional on sponsor's right to revoke).

Respondents contend, suggest otherwise. (*See* Opp. at 3-4)[2] The court stated in *Carr* that "the participants in [top hat] plans may enforce the terms of their plans under the federal common law rules of unilateral contract generally applicable to pension plans, *so long as the asserted unilateral contract rights are found in the terms of plan documents themselves*." *Id.* (emphasis added) Therefore, under *Carr*, Respondents should be able to recover their top hat plan benefits only if the written terms of the Plans reasonably can be construed to vest the participants in these benefits upon retirement. Resolution of that issue depends on the selection of the appropriate common law rule of plan construction.

Contrary to Respondents' assertions, in applying the federal common law to construe the Plans, the Third Circuit relied primarily on authorities for construing ordinary welfare plans. For example, the court repeatedly cited from *Mellon Bank, N.A. v. Aetna Business Credit, Inc.*, 619 F.2d 1001 (3d Cir. 1980),[3] as well as several decisions that rely on *Mellon Bank*'s methodology in construing welfare plans, as support for rejecting

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[2] *Carr*'s endorsement of unilateral contact principles to construe a top hat plan was based, not on the inapplicability of ERISA's writing requirement, but rather on the resemblance that the plan bore to a pension plan. *See Carr*, 921 F. Supp. at 1485. That resemblance, however, is inapplicable here in light of the various welfare-type benefits included in the Plans. (*See* Pet. at 3-4; A-86-92) There is thus no reason for applying unilateral contract principles here that is not equally applicable to welfare plans.

[3] In support of their contention that there is no conflict among the circuits regarding the use of forum law, Respondents mistakenly treat the *Mellon Bank* line of authority as if it is based on federal, rather than state law. Although courts in the Third Circuit subsequently relied on *Mellon Bank* to formulate the federal common law of contract construction in ERISA cases, *see, e.g., Taylor*, 933 F.2d at 1234, the original *Mellon Bank* decision merely applied the state law of Pennsylvania in a federal diversity action. *Mellon Bank*, 619 F.2d at 1005.

a "four corners" approach to contract interpretation in favor of a methodology that more liberally resorts to extrinsic evidence (*see* A-11, A-13). *See, e.g., Teamsters Indus. Employees Welfare Fund v. Rolls-Royce Motor Cars, Inc.*, 989 F.2d 132, 135 (3d Cir.1993); *Alexander v. Primerica Holdings, Inc.*, 967 F.2d 90, 93 (3d Cir. 1992); *Sheet Metal Workers v. 2300 Group, Inc.*, 949 F.2d 1274, 1284 (3d Cir.1991); *Taylor v. Continental Group Change in Control Severance Pay Plan*, 933 F.2d 1227, 1234 (3d Cir.1991). As the authorities cited in the Petition demonstrate (*see* Pet. at 13-17), however, *Mellon Bank*'s methodology has not been universally adopted. To the contrary, the decision lies at the heart of the conflict on plan construction that has divided the circuit courts. (*Id.*)

The fact that the Third Circuit may have exhibited a greater inclination to endorse liberal principles of contract construction because a top hat plan was at issue here, as a comparison of the decision below with *In re Unisys Corp. Retiree Medical Benefit "ERISA" Litigation*, 58 F.3d 896 (3d Cir. 1995), *cert. denied*, 116 S. Ct. 1316 (1996) ("*Unisys*") suggests, does not render the decision less suitable for addressing the broader conflicts among the circuits on plan construction. To the contrary, it demonstrates the risks presented if the conflict is not resolved promptly. For reasons already stated in New Valley's petition, which Respondents do not refute, federal common law was used in this case to reach a result that contradicts the goals underlying ERISA, by elevating the rights of top hat plan participants above those of ordinary welfare plan participants. Absent a uniform rule governing plan construction, decisions like these threaten to further undermine the integrity of ERISA's civil enforcement scheme.

In short, there is nothing so unique about the Third Circuit's decision that should render it unsuitable for Supreme Court review. If anything, the fact that the plans at issue were top hat plans serves to underscore the need for such review.

II.

RESPONDENTS HAVE FAILED TO REFUTE THE EXISTENCE OF CONFLICTS AMONG THE CIRCUIT COURTS OVER PLAN CONSTRUCTION AND RESORT TO FEDERAL COMMON LAW

In its petition, New Valley identified three related issues that control the outcome of this case and as to which the circuit courts are deeply divided: (i) whether to consider extrinsic evidence in construing a plan containing a facially unambiguous reservation-of-rights clause; (ii) whether, and under what circumstances, to apply federal common law principles of unilateral contract and illusory promise in construing employee benefit plans; and (iii) whether, in formulating an ERISA federal common law rule, courts should incorporate the common law of the forum state. With respect to each of these issues, Respondents contest the existence of a conflict through a selective and distorted characterization of the case law cited in the Petition, which ultimately does not alter the existence of the conflict.

Conflict Over The Use Of Extrinsic Evidence

In support of their contention that there is no conflict regarding the use of extrinsic evidence, Respondents assert that the Seventh Circuit's decision in *Murphy v. Keystone Steel & Wire Co.*, 61 F.3d 560 (7th Cir. 1995), and the Third Circuit's decision in *Schoonejongen v. Curtiss-Wright*, 18 F.3d 1034 (3d Cir. 1994), *rev'd and remanded on other grounds*, 115 S. Ct. 1223 (1995), did not apply a "four corners" approach to plan interpretation, but rather construed the plans based on "the circumstances as developed at trial[.]" (Opp. at 5) There was no trial in *Murphy*, however. The proper construction of the plan was determined on motion for summary judgment, based exclusively on an examination of the plan language and the reservation-of-rights clause contained in the collective bargaining agreement pursuant to which the plan was sponsored. Although a trial was conducted in *Schoonejongen*, the Third Circuit stated on appeal that

> [its] conclusion [that Curtiss-Wright had a reserved right to amend] [was] a complete answer to th[e contractual vesting] argument. Even if the plan contained unambiguous assurances that all retirees would have health insurance benefits for so long as Curtiss-Wright maintained a post-retirement health insurance program, the general reserved right to amend the terms of the plan in whole or in part would render the right of any retiree or group of retirees terminable by the adoption of a legally effective amendment.

18 F.3d at 1042.

When subsequently confronted with a reservation-of-rights clause similar to the clause in *Schoonejongen* and identical to the clause at issue here, the Third Circuit ruled explicitly that the clause foreclosed the necessity of a trial because

> plans [that] use[] terms such as "lifetime" or "for life" to describe the duration of retiree medical benefits, while at the same time expressly reserving the company's right to terminate the plans under which those benefits were provided, d[o] not render the plans "internally inconsistent" and therefore ambiguous . . . .

In re Unisys Corp. Retiree Medical Benefit "ERISA" Litigation, 58 F.3d 896, 903-04 (3d Cir. 1995), *cert. denied*, 116 S. Ct. 1316 (1996). In so holding, the court applied the same reasoning employed by the Fourth Circuit in *Gable v. Sweetheart Cup Co.*, 35 F.3d 851 (4th Cir. 1994), *cert. denied*, 115 S. Ct. 1442 (1995) and the Eleventh Circuit in *Alday v. Container Corp.*, 906 F.2d 660 (11th Cir. 1990), *cert. denied*, 498 U.S. 1026 (1991), neither of which is even addressed by Respondents. There can be no disputing that the approach taken in these cases differs markedly from the approach taken in *Jensen v. SIPCO, Inc.*, 38 F.3d 945 (8th Cir. 1994), *cert. denied*, 115 S. Ct. 1428 (1995) and *Armistead v. Vernitron*, 944 F.2d 1287 (6th Cir. 1991),

which, as Respondents concede (*see* Opp. at 6), "rely heavily" on extrinsic evidence. *See also Chiles v. Ceridian Corp.*, 95 F.3d 1505 (10th Cir. 1996) (identifying split among circuits on issue of whether reservation-of-rights clause trumps promise of benefits so as to render inappropriate resort to extrinsic evidence).

Conflict Over The Use Of Federal Common Law Principles

Respondents also mischaracterize *Murphy* insofar as they dispute that the decision rejects the applicability of the unilateral contract principles endorsed here by the Third Circuit. Confronted with claimants' argument that their "exit agreements" with the company constituted unilateral contracts which vested them in their health benefits at retirement, the Seventh Circuit ruled that no such vesting could occur in the presence of a reservation-of-rights clause. *Murphy*, 61 F.3d at 564.

The use of unilateral contract principles has, in any event, been rejected by the Second Circuit in *Reichelt v. Emhart Corp.*, 921 F.2d 425, 432 (2d Cir.1990) (explaining that application of unilateral contract theory "would nullify Congress's determination in structuring ERISA that welfare benefit plans such as severance plans should be exempted from the stringent vesting requirements applicable to pension benefit plans"), *cert. denied*, 501 U.S. 1232 (1991), as well as by the Eighth and Ninth Circuits in *DeGeare v. Alpha Portland Indus.*, 837 F.2d 812 (8th Cir. 1988) and *Fielding v. Int'l Harvester Co.*, 815 F.2d 1254 (9th Cir. 1987). In fact, *DeGeare* and *Fielding* expressly rejected the argument, advanced by Respondents here (*see* Opp. at 5-6), that a promise of lifetime medical benefits made conditional on the sponsor's reserved right to terminate such benefits is somehow illusory. *See Fielding*, 815 F.2d at 1257; *DeGeare*, 652 F. Supp. at 961, *aff'd*, 837 F.2d 812 (8th Cir. 1988). Thus, there can be no disputing that the circuit courts are divided in their use of the common law principles endorsed here by the Third Circuit.

Conflict Over The Use Of Forum Law

Finally, Respondents' contention that there is no conflict over the use of forum law to fashion the federal common law of ERISA is belied by the numerous authorities that not only have identified and discussed this conflict, but have also commented on the dangers that it presents to the fulfillment of ERISA's congressional goals. *See, e.g., Hughes v. Boston Mutual Life Ins. Co.*, 26 F.3d 264, 268-69 (1st Cir. 1994) (discussing conflict among circuits on question of whether adoption of state *contra proferentem* rule should be incorporated into ERISA federal common law rules of plan interpretation); *McGee v. Equicor-Equitable HCA Corporation*, 953 F.2d 1192, 1200 (10th Cir. 1992) (observing that circuits are split on whether principle of *contra proferentem* applies to interpretation of ERISA contracts); *see also* Flint, G., *ERISA - Reformulating the Federal Common Law for Plan Interpretation*, 32 San Diego L. Rev. 955 (Fall 1995) (addressing conflict among circuits on whether state law should ever provide basis for fashioning rules of plan interpretation in light of ERISA's broad preemptive sweep).

In short, there is no disputing the existence of serious rifts among the circuit courts in connection with the construction of plan reservation-of-rights clauses and the formulation and use of federal common law rules of construction. The resolution of those conflicts would have a direct bearing on the validity of the Third Circuit's decision below.

CONCLUSION

For all the foregoing reasons, the petition for writ of certiorari should be granted.

Respectfully submitted,

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